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# Statement Before The Governor's Commission on Waste, Fraud and Abuse

**By**

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I appreciate the opportunity and am grateful for the invitation to spend some time with you this morning, and to share some thoughts concerning our state's unemployment insurance system.

My name is Bill G. Smith, and I am State Director for the National Federation of Independent Business. The NFIB has nearly over 370,000 members nationwide, including more than 12,000 member firms located here in Wisconsin.

I was asked to share some comments on some options related to the state's unemployment compensation system. You will note that the word options was listed on your agenda – not solutions or even recommendations. I will leave that to the experts including the staff at the Department of Workforce Development, members of the Legislature and Congress, and Wisconsin's Unemployment Advisory Council.

## 1. Provide short term relief from Federal Unemployment Tax Penalties

The first step, and this really isn't an option but rather an urgent need, is to get unemployed workers back to work.

It is no exaggeration that the UI employer financed system is in the worst financial condition since its inception. The federal extended unemployment compensation account from which regular extended benefits are funded is in deficit. The federal unemployment account is broke and the states have run out of money to make benefit payments.

According to projections by the U.S. Department of Labor, there will be very large amounts borrowed from the Federal Unemployment Account over the next few years.

The balance of outstanding loans are projected to reach $93 billion in FY 2013. A total of 40 states are projected to borrow from the fund.

In this environment in which UI payroll taxes are increasing and will continue to increase for a number of years, employers are hesitant to create new jobs or rehire employees because of the uncertainty and size of payroll tax burdens. An immediate positive step would be to provide relief from FUTA tax penalties on employers in states like Wisconsin that are borrowing to pay unemployment compensation benefits.

The waiver of interest on loans to states to pay unemployment compensation should be extended through 2012 and 2013 in the short term to plan to help states restore solvency and to implement solvency legislation within a reasonable timeframe.

## 2. <u>Develop Intiatives That Are Most Effective In Assisting Unemployed Workers In Returning To Work</u>

An analysis of the makeup of the 5.6 million long term unemployed workers and those who are likely to exhaust unemployment compensation and are currently claiming state unemployment compensation is needed to determine the most cost effective ways to assist them in returning to work. Once there is a determination of the size of the population to be served and an evaluation of resources needed, assessments of workers should form the basis on which to determine whether the individuals are in need of job search, training, and/or support services.

In some cases there will be barriers that must be addressed (e.g. illiteracy, drug abuse, child care needs). Partnering with public and private workforce agencies may be needed.

## 3. <u>Job Search and Reemployment Services</u>

Workers with skills in demand can immediately benefit from job search and reemployment services.

Employers are typically not aware of the services or have made independent outplacement and reemployment service plans for displaced workers. With appropriate consultation, private/public partnerships can serve to reduce the number of workers who become unemployed, reduce the duration of unemployment, and reduce the cost to employers.

It has been well established that effective job search reduces the number of weeks that individuals remain on unemployment compensation and also serves to more quickly fill the staffing needs of employers. The use of web based job search systems and public/private partnerships has demonstrated that greater efficiency and effectiveness in job search can be a win/win by reducing the duration of unemployment compensation, and returning unemployed workers to the workforce more quickly.

## 4. Targeted Training

The assessment and referral to training and placement of unemployed workers can be effective in enabling workers to find new work. Employer based programs, such as customized training, on the job training that permit individuals to work as employees or trainees in anticipation of long-term employment are the most effective in moving unemployed workers into training which is likely to lead to employment.

The July 2009 report of the President's Council of Economic Advisers "Preparing the Workers of Today for the Jobs of Tomorrow", identified the elements of more effective post-high school education and training and reported that "The curricula for occupationally-oriented programs should be developed in close collaboration with local employers and other workforce stakeholders".

Active participation by employers is the key to successful training as employers ultimately make the hiring decisions. Targeted initiatives in the areas of health services, manufacturing, and other growth areas make sense in the current economy as a way to meet employer needs and to reduce unemployment.

The leveraging of public funding across program areas as well as private funding driven by employers who are making hiring decisions can be extremely effective in developing the training and support needed to return unemployed workers to work.

## 5. Geographic Relocation

Deep recessions historically result in significant geographic shifts in the availability of employment as labor markets adjust to the emerging areas of growth and employment levels in some labor markets that do not return to previous levels.

Individuals remaining unemployed for extended periods should be encouraged to consider relocating to other geographic locations in which employment matches their skills and abilities is available.

## 6. Improve Accuracy and Integrity

One of the most effective ways to get unemployed workers back to work is for them to take responsibility personally and to be motivated to take jobs that are available. A number of administrative and policy measures have been shown to be effective in motivating unemployed workers to take responsibility.

During the recession it has been understandably difficult for state UI administrative staff to focus on benefit payment control, fraud and overpayments when the priority has been to assure that the growing number of unemployed workers were able to complete their applications, weekly claims forms and be paid quickly.

Paying attention to whether individuals are actively seeking work and making accurate benefit determinations sends the signal to unemployed workers that they are expected to take the initiative to actively seek work and be accountable.

Targeted administrative funding is essential immediately. The longer the lack of funds dedicated to integrity functions, the more difficult it will be to assure active work search, avoid inaccurate payments, or effectively collect overpayments. Also, immediate attention and publicity of the fact that the agency is cracking down on fraud serves as a deterrent to fraud. Funding is needed to procure detection and collection systems and to dedicate staffing to increase the capacity and the integrity of the system.

## 7. Examine the Impact of the American Recovery and Reinvestment Act (ARRA) Unemployment Compensation Related Provisions

The Emergency Unemployment Compensation (EUC), the Federal Additional Compensation (FAC) and the 100% Reimbursement of state benefit payments for regular federal extended benefits provided for in the American Recovery and Reinvestment Act (ARRA) have served to provide needed support for unemployed workers who became unemployed due to the recession. They may also have had the unintended consequence of contributing to the increase in the duration of unemployment compensation and restricting states in the addressing of solvency of their funds.

A comparison of the average duration of weeks of state unemployment compensation from the fourth quarter of 2008 to the fourth quarter of 2009 shows a dramatic increase in average duration nationally from 14.9 weeks of benefits to 18.8 weeks of benefits.

A rough rule of thumb used by the Congressional Budget Office (CBO) is that making benefits available to all regular UI recipients for an additional 13 weeks increases their average duration of unemployment by about two weeks and that increasing UI benefit levels by 10 percent increases the average duration of unemployment by about one week.

The FAC may have the effect of increasing the cost of labor, particularly as job opportunities return. A $25 per week addition is nearly a 10 percent increase on average, and for claimants with lower wages this additional weekly payment may be a disincentive to accepting work as it becomes more readily available.

## LONG TERM STRATEGIES

## 1. Conduct a Study and Make Recommendations

A careful study of UI system solvency is needed with implementation to begin as the economy fully recovers. The study should include a review of the major revenue and cost drivers in the current system, including 1) state and federal unemployment tax bases, 2) tax rates, 3) adjustments in tax and benefit amounts, 4) benefit eligibility requirements and conditions of payment, 5) weekly benefit amounts and duration, 6) debt management,

7) extended benefit trigger provisions, 8) circumstances under which Federal loans may be available to states and terms of repayment, 9) clear delineation of the scope of the employer financed unemployment insurance system within the larger context of social safety net programs, and 10) proper administrative financing, including targeted administrative funding for integrity.

## 2. Experience Rating

A critical element of the Federal/State unemployment compensation system is the requirement that employer contribution rates under state law must be based on factors related to unemployment. This requirement assures greater employer participation in determinations with respect to the allowance of unemployment compensation benefits and weekly determinations of eligibility because employers have an economic interest in whether their accounts are charged and their contribution rates are increased. The requirement adds integrity to the system by increasing the likelihood that UI agencies will have the information needed to determine fraud and overpayments.

The experience rated system assists in avoiding erroneous payments and preserving unemployment trust fund dollars for those who properly qualify.

It also enables employers to project unemployment compensation costs, encourages proper management of human resources, and provides a fair basis upon which to distribute the cost of state unemployment compensation among the employers participating in the system.

The experience rated system works best when there is a direct relationship between unemployment claims experience and contribution rates. Artificial minimums or maximums may result in non-experienced based cost shifting.

There should also be an evaluation of the so called "non-charged" benefits that have increased over the years, undercutting the experience rated features of the program.

## 3. Long Term Solvency and Debt Management

The size of the state unemployment trust fund debt is so great in most states that a goal to meet solvency standards suggested by USDOL, or the existing state law solvency standards within five years, would require tax increases and/or benefit cuts which are simply too great, and would destroy the creation of jobs or severely limit the primary safety net for the state workforce.

The review of possible solutions to the long term problem should include an examination of the write off of outstanding loans, while addressing the need to reset the size of the program and the financing of it.

## 4. Avoid Job Killing Increases in Federal and State Unemployment Taxes

Employers decide to create jobs and maintain higher levels of employment based not only on the demand for goods and services, but also on the costs associated with employees. Unemployment insurance has become a very significant cost, especially for labor intensive smaller businesses.

State unemployment taxes will likely be increasing in the next two years and may stay at a much higher rate for a decade before solvency returns to state UI trust funds. Employers with relatively low state unemployment taxes will likely experience even greater percentage increases. As a point of comparison, for 1982, the state unemployment tax as a percent of total wages was 1.759%, nearly triple the state UI taxes as a percent of total wages of 0.61% as of the second quarter of 2009. Increases of this size will adversely impact job creation. A plan to address taxes and benefits while managing the outstanding debt is needed to reach job creation goals.

## 5. Reduce Unemployment Compensation Pay-Out

As the economy recovers and jobs become more widely available, and as the unemployment rate declines, there will be a reduction in benefit pay out. At the same time increases in unemployment tax revenue will result from higher payrolls, experience rated tax increases and solvency taxes. Although the trend lines will improve, without carefully assessing the long term cost of benefits and taxes and making appropriate adjustments, history will repeat itself with benefit obligations in the next recession that will once again outstrip our ability to pay.

Since the 1980s the scope of the unemployment insurance system in a number of states has been expanded, and benefit payout associated with these expansions has contributed to the insolvency of the state unemployment benefit accounts, and ultimately the depletion of the Federal Unemployment Account.

Areas to review for reductions include monetary qualifying requirements, dependency allowances, weekly benefit amounts, waiting periods, work search and availability requirements, conditions of removal of disqualifications, overpayment collections, and fraud.

In some instances, expanded benefit provisions were enacted with a provision socializing the cost or relying on temporary funding. Unfortunately, although benefit costs may not be charged to a specific employer account, the increased cost to the state unemployment trust fund nonetheless must be paid with taxes paid by all employers or cuts in other benefit provisions. Also, long term costs associated with expansions that were temporarily funded nonetheless must be accounted for in determining long term solvency and making adjustments.

6. **<u>Keep the role of the UI program as it was established</u>**

As it was enacted and signed by President Roosevelt in 1935, the unemployment insurance program was smaller in scope than it is today. The program did not include a federal extended benefit program and there was no requirement that individuals working for non-profit agencies or state and local governments be covered for state unemployment compensation. Legislation enabling states to borrow from federal funds to pay unemployment benefits did not begin until the late 1950s and the Federal/State Extended Unemployment Compensation Act was not enacted until 1970.

At inception, however, unemployment insurance was a more important part of the national social safety net because the workforce relied primarily on wages and savings for economic security. The UI system was established as a temporary partial wage replacement program for workers who became unemployed through no fault of their own in connection with their work, available for work and actively seeking work. That purpose and focus should be maintained.

Unemployment Insurance is much more important in providing economic security for individuals who rely principally on their employment and wages for support. The UI program serves a very specific purpose that employers are willing to support with dedicated employer tax dollars.

However, in developing plans to assist unemployed workers in returning to work, the UI program should be used in conjunction with workforce programs dedicated to provide job search, reemployment and training services that may be funded from other sources, but are aligned to provide economic security and effective workforce services to the benefit of the individual, employers, and economic development.

## CONCLUSION

The status of the slowly recovering economy dictates that, although the state and federal trust funds are insolvent, we must first do no harm to discourage job creation and economic recovery. The federal penalties that would otherwise be imposed in the form of Title XII loan interest and the FUTA offset credit penalty should be waived for three years to avoid dampening the creation of jobs and the economic recovery.

States should be properly funded to work with unemployed workers and employers to improve initiatives and services designed to return unemployed claimants back to work.

Training initiatives should be closely coordinated with employers in developing customized training, apprenticeships and other employer based training that leads to employment.

Training and services provided for unemployed claimants should also be coordinated with providers in the private sector and with other workforce programs aligned to put claimants back to work.

A comprehensive study of the primary cost and revenue drivers of the federal and state unemployment system should be conducted with a view toward identifying solutions that recognize the need to avoid tax increases that negatively impact job creation, and reduce long term benefit pay-out without impairing the mission of the program, which is to provide temporary partial wage replacement for unemployed workers who become unemployed through no fault of their own in connection with their work.

I want to thank you for the opportunity to share some comments with you, as well as commend you for working to identify and hopefully eliminate waste, fraud and abuse in our government.